

EX PARTE OR LATE FILED



RECEIVED

JAN - 4 1995

FEDERAL COMMUNICATIONS COMMISSION  
OFFICE OF THE SECRETARY

Whitney Hatch  
Assistant Vice President  
Regulatory Affairs

GTE Service Corporation  
1850 M Street, N.W., Suite 1200  
Washington, D.C. 20036  
202 463-5290

January 4, 1995

Mr. William F. Caton, Acting Secretary  
Federal Communications Commission  
1919 M Street, N.W., Room 222  
Washington, D.C. 20554

**EX PARTE:** CC Docket No. - 94-1

ORIGINAL - NOT A COPY

Dear Mr. Caton:

Today a representative of GTE Service Corporation met with Lauren 'Pete' Belvin of Commissioner Quello's office to discuss GTE's position in the above-captioned proceeding. The discussion covered issues raised in this proceeding by GTE in its filings and in materials submitted previously to the record in ex parte filings. The attached hand-out was used to augment the discussion.

Please call me if you have any questions.

Sincerely,

Whitney Hatch

c: L. Belvin

No. of Copies rec'd  
List ABCDE

041

RECEIVED

JAN - 4 1995

FEDERAL COMMUNICATIONS COMMISSION  
OFFICE OF THE SECRETARY

Review of Price Cap Issues

GTE

- 1) Plan for Commission action
- 2) Rate structure reform
- 3) Adaptive regulation
  - a) Concepts
  - b) Implementation
- 4) Measuring competition
- 5) Price cap mechanics
- 6) Timing

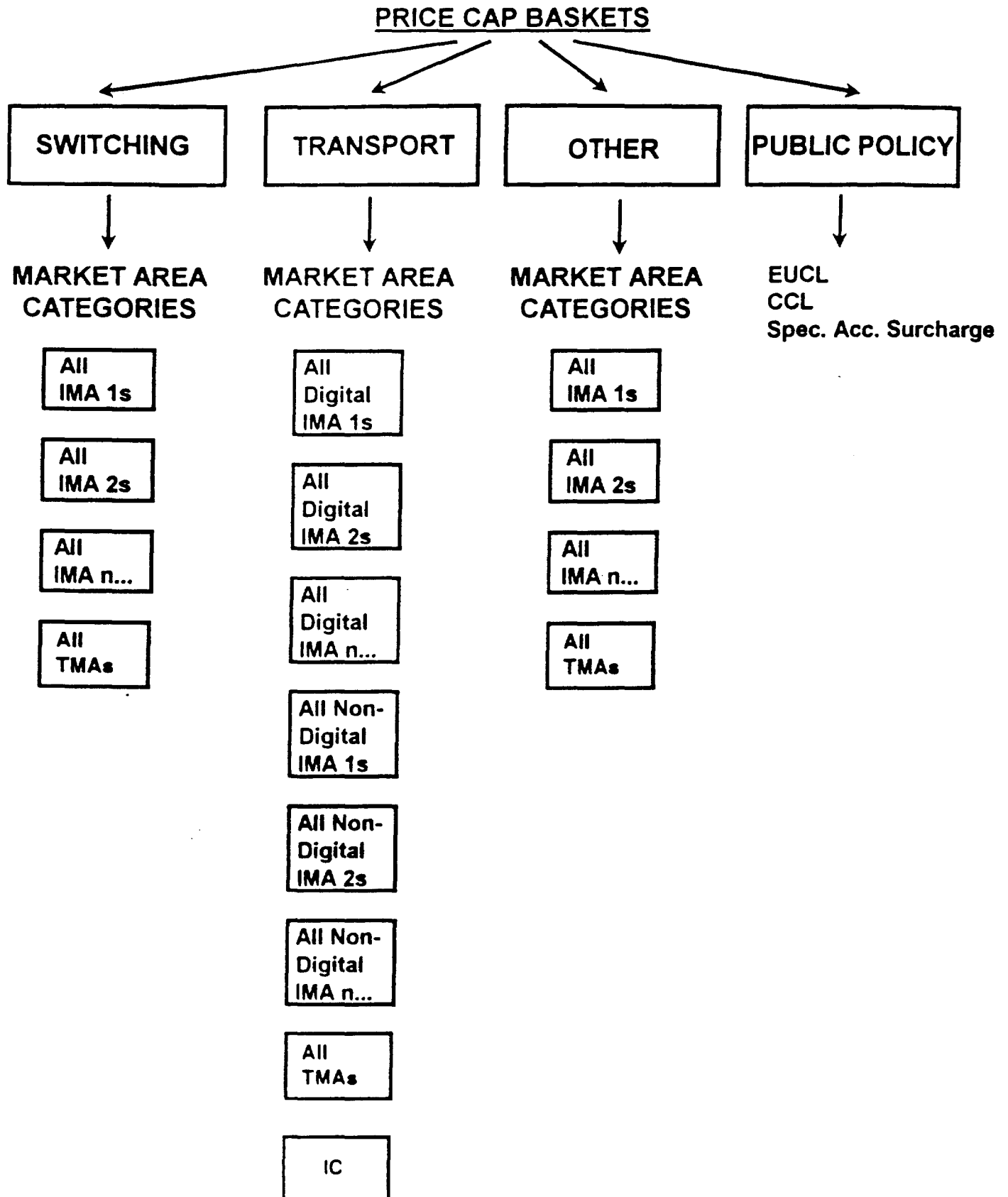
## Plan for Commission Action

- 1) Initial Order on Price Caps (February 1995)
  - a) Action on price cap mechanics
    - Productivity, sharing, etc
  - b) Finding on need for access reform
    - Rate structure, adaptive framework
    - Initial steps if possible
  - c) Further Notice on access reform issues
    - Time line for resolution
- 2) NPRM on Universal Service (May-June 1995)
  - a) Comprehensive review
    - Not just USF
- 3) Complete FNPRM on access reform (August 1995)
  - a) Adopt new rate structure, adaptive framework
  - b) Provide basis for action on universal service, other issues

## Rate Structure Reform

- 1) Current Part 69 rules are outgrowth of 1983 access charge plan
  - Not suitable for new environment:
    - rapid technological change
    - access competition
- 2) Rules impede:
  - New Service introduction
  - Effective competitive response
- 3) Two problems:
  - a) Need for waiver or rule change
    - Reverses presumption in favor of new services in Section 7 of Act
  - b) Classification problem
    - New services don't fit
- 4) Solution:
  - a) Commission should not define most rate elements
    - Hopeless task in changing market
    - Not needed for price caps
      - No Part 69 cost allocations
  - b) Codified Public Policy elements for specific Commission programs (such as EUCL)

# PROPOSED BASKET DESIGN FOR PRICE CAP LECS



## Adaptive Framework of Regulation

- 1) Need mechanism to adjust degree of regulation to match degree of competition in each access market

Key elements:

- Definition of Market Area
- Market Area Classification
- Criteria for Classification
- Pricing Rules by Market Area

- 2) Definition of Market Area

- a) Access, not Local
- b) Narrow geographically
- c) Broad in terms of products

USTA proposes: Geographic area served by one or more wire centers

- Smallest unit of observation
- Pre - existing entity
- Matches existing billing, ordering systems

3) Market Area Classification

a) Three levels of markets:

- Initial Market Area (IMA)
- Transitional Market Area (TMA)
- Competitive Market Area (CMA)

b) Builds on existing zone plan

- Each zone becomes an IMA

c) Within an IMA, wire centers may become part of a TMA

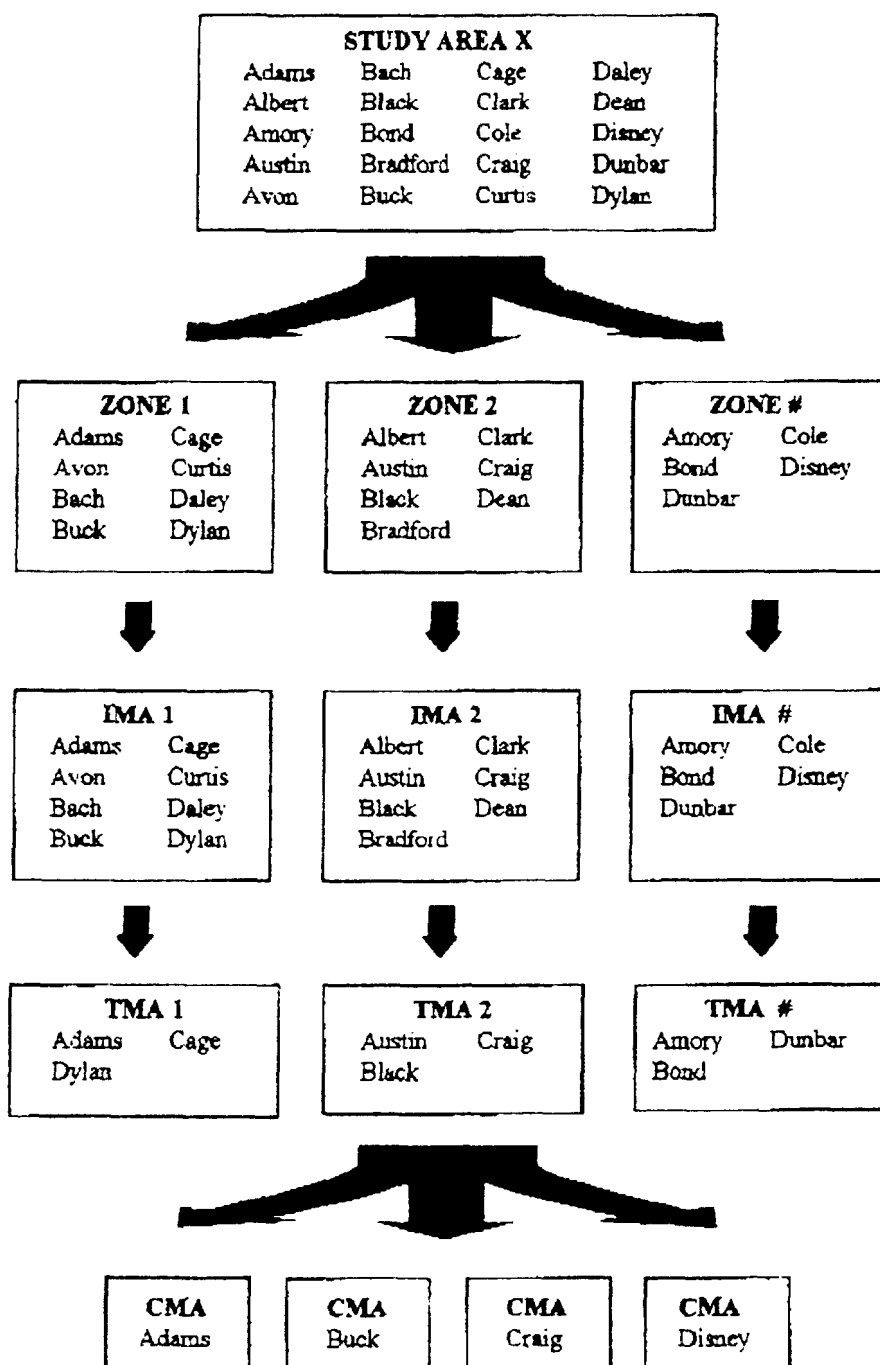
- Upon showing of presence of a competitor

d) Individual wire center may be designated as a CMA

- Upon showing that competition is sufficient to limit market power
- Alternative facilities in place to make service available for customers representing 25% of demand
- Showing may be made
  - For all access services
  - For one or more price cap baskets
  - For multiline customers only (GTE proposal)

# Transition of Market Area Classification

---





## PROPOSED NOTICE INTERVALS

TYPE OF FILING	MARKET AREA CLASSIFICATION		
	IMA	TMA	CMA
Annual Tariff	90 days	90 days	N/A
Price Change - Within Band	14 days	14 days	N/A
Price Change - Above Band	120 days	120 days	N/A
Price Change - Below Band	45 days	45 days	N/A
Price Change - CMA	N/A	N/A	7 days
New Services	45 days	21 days	14 days
Restructure	21 days	21 days	14 days
Contract-Based Tariffs	N/A	21 days	14 days
Services Excluded From Price Cap Regulation	45 days	21 days	14 days
Market Area Classification	21 days	21 days	21 days
Other	21 days	21 days	14 days

## PROPOSED SUPPORT REQUIREMENTS for PRICE CAP LECs

Proposed Support Requirements for Price Cap LECs						
Type of Filing	Cost Support Requirements			Demand Support Requirements		
	IMA	TMA	CMA	IMA	TMA	CMA
In Band	None	None	N/A	Yes	Yes	N/A
Below Band	Yes	Yes	N/A	Yes	Yes	N/A
Annual	None	None	N/A	Yes	Yes	N/A
Restructure	None	None	N/A	Yes	Yes	N/A
New Services	Yes	Yes	None	Yes	Yes	None
Contract Services	N/A	Yes	None	N/A	Yes	None
Services Excluded From Price Caps	Yes	Yes	None	Yes	Yes	None

**None:** Indicates cost and/or demand support is not required for the particular type of filing within that market area.

**N/A:** Indicates the particular type of filing is not applicable for that market area.

**Yes:** Indicates varying degrees of cost and/or demand support is required for the particular type of filing within that market area.

#### 4) Criteria for streamlining

##### a) Addressability

- Measures market power directly
- Forward-looking indicator
- Asks whether customers have choices
- Captures ability (capacity) to supply
- Based on real, not potential, competition
  - Facilities in place

##### b) Other proposed criteria are not reasonable

- Market share
  - Measures choices customers have made, rather than those they have available
  - Not directly related to market power
  - Backward-looking: establishes pricing signals only after market decisions have been made
  - Presupposes market outcome
    - "Reserves" portion of market for entrants
- "Structural" preconditions
  - No significant barriers to access markets
  - Proposed conditions relate to local, not access, competition
  - If addressability condition met, entry has already occurred

5) Pricing rules based on market classification

- IMA: price caps, banding
- TMA: price caps, looser bands
  - Contract-based tariffs in response to RFP
- CMA: No price caps
  - Contract-based tariffs for all services
  - Still tariffed, Title II services

- 6) Proposed rules effectively protect consumers, competition
  - a) Prices too high
    - Caps where market power still exists
  - b) Prices too low (predation)
    - Price floors at incremental cost
    - Recoupment unlikely
      - Increasing competition
      - Streamlining only when competitors have sunk capacity
  - c) Cross-subsidy
    - Caps on less competitive markets
      - Independent of events in more competitive markets -- because no sharing or LFAM
    - Floors on all rates
  - d) Vertical price squeeze
    - Addressability criterion does not rely on interconnection
    - Streamlining only when customers have choices through competitors' own facilities
  - e) Discrimination
    - Existing policies on discrimination, resale, sharing continue to apply
    - Rates not discriminatory simply because they are different

**The Commission Should Adopt  
an Adaptive Framework Now**

- **Benefits of adaptive framework**
  - Establishes clear ground rules for competition up front
    - Provides reasonable expectations for all players
    - Undistorted market signals to guide entry, investment, purchase decisions
    - Efficient development of NII
    - Immediate benefit in all markets
  - Replicates market outcome
    - In competitive markets, by allowing market forces to work
      - Consumers benefit from lower prices, more effective competition, wider choice of services.
    - In less competitive markets, by protecting consumers
      - Effective protection from abuse of market power, anticompetitive behavior
  - Facilitates introduction of new services
  - Allows prompt, efficient regulatory response
    - No need for new proceeding every year to assess changes in market
- **There is no downside to adopting a framework now**
  - Streamlining would be granted only where LEC has shown that criteria are met
- **Time to establish trigger mechanism and ground rules for competition is now**
  - Not after investment decisions have already been made
  - To permit rational development of competition

## Price Cap Mechanics

- 1) Productivity
  - Based on TFP as measured by Christensen
  - Incorporate moving average adjustment
- 2) Sharing
  - Essential for access reform
  - Better incentives, protection
- 3) Exogenous
- 4) First steps on baskets, bands, pricing rules
  - Consistent with access reform
  - Avoid need to redo later